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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

STATE OF SOUTH CAROLINA,
*Plaintiff,*

vs.

DONALD T. REGAN, SECRETARY OF THE TREASURY OF THE UNITED STATES OF AMERICA,
*Defendant.*

# AMICUS CURIAE BRIEF OF TEXAS, ALASKA, ARIZONA, GEORGIA, INDIANA, IOWA, LOUISIANA, MARYLAND, MISSISSIPPI, MISSOURI, MONTANA, NEVADA, NEW HAMPSHIRE, NORTH CAROLINA, NORTH DAKOTA, OHIO, OKLAHOMA, PENNSYLVANIA, RHODE ISLAND, TENNESSEE, VERMONT, VIRGINIA, WISCONSIN AND WYOMING

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## INTEREST OF AMICUS CURIAE

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The interest of *amicus curiae* filed pursuant to Rule 36.4 of the Rules of the Supreme Court of the United States for Texas, Alaska, Arizona, Georgia, Indiana, Iowa, Louisiana, Maryland, Mississippi, Missouri, Montana, Nevada, New Hampshire, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, Tennessee, Vermont, Virginia, Wisconsin and Wyoming is in elaborating the consequences of (1) the Court's refusal to entertain South Carolina's Motion to the Original Jurisdiction of the Court and (2) the implementation of Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 requiring that municipal bonds be issued in registered form in order that the interest thereon be exempt from Federal income taxation.

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*May _____, 1983.*

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# ARGUMENT

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## QUESTIONS PRESENTED

I. Is there a serious controversy upon which the Court should exercise its Original Jurisdiction?

   A. Is the State as State damaged?

   B. Does the State have an interest in redressing the damage done to its political subdivisions?

II. Is the Supreme Court the proper forum for the complaint which South Carolina has moved for leave to file?

III. Is the implementation of Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act an unconstitutional exercise of Congressional taxing power?

## JURISDICTION

The sovereign State of South Carolina has invoked the original jurisdiction of the Court according to the jurisdictional grant bestowed in Article III, Section 2 of the United States Constitution providing original jurisdiction in a case or controversy between a State and a citizen of another State. South Carolina, as a sovereign State in the federal system seeks redress against Donald T. Regan, Secretary of the Treasury of the United States, currently a resident of the State of Virginia. The States of Texas, Alaska, Arizona, Georgia, Indiana, Iowa, Louisiana, Maryland, Mississippi, Missouri, Montana, Nevada, New Hampshire, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, Tennessee, Vermont, Virginia, Wisconsin and Wyoming, consistent with Rules of the Supreme Court, Rule 36.4 files this Brief of Amicus Curiae in the action of South Carolina.

## CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Tenth Amendment to the United States Constitution provides:

> The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

The Sixteenth Amendment to the United States Constitution provides:

> **The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.**

Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 provides:

(b) OTHER OBLIGATIONS. —

(1) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.—Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

'(j) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.—

'(1) IN GENERAL.—Nothing in subsection (a) or in any other provision of law shall be construed to provide an exemption from Federal income tax for interest on any registration-required obligation unless the obligation is in registered form.

'(2) REGISTRATION-REQUIRED OBLIGATION.—The term "registration-required obligation means any obligation other than an obligation which—

'(A) is not of a type offered to the public,

'(B) has a maturity (at issue) of not more than 1 year or

'(C) is described in section 163(f)(2)(B).

'(3) SPECIAL RULES.—

'(A) BOOK ENTRIES PERMITTED.—For purposes of paragraph (1), a book entry obligation shall be treated as in registered form if the right to the principal of, and stated interest on, such obligation may be transferred only through a book entry consistent with regulations prescribed by the Secretary.

'(B) NOMINEES.—The secretary shall prescribe such regulations as may be necessary to carry out the purpose of paragraph (1) where there is a nominee or chain of nominees.'

## STATEMENT

On February 9, 1983, the State of South Carolina moved for leave to file a complaint to the original jurisdiction of the Court contesting the constitutionality of Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) because it infringes on rights of state sovereignty guaranteed by the Tenth Amendment to the United States Constitution. Section 310(b)(1) provides that, in order to be exempt from Federal income taxation, any obligation of a State or municipal issuer must be in registered form effective July 1, 1983. Donald T. Regan is responsible for administering and enforcing Section 310(b)(1) under the dictate of 26 U.S.C. Section 7801. South Carolina has moved to the Court's original jurisdiction as a sovereign in the federal system seeking redress against the acts of a citizen of a foreign state. Texas, Alaska, Arizona, Georgia, Indiana, Iowa, Louisiana, Maryland, Mississippi, Missouri, Montana, Nevada, New Hampshire, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, Rhode Island, Tennessee, Vermont, Virginia, Wisconsin and Wyoming, herein file this brief of *amicus curiae* both as to the jurisdictional question and on the merits of the claim.

## SUMMARY OF ARGUMENT

South Carolina's action puts into issue the constitutionality of Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act of 1982 as an attempt to impermissibly infringe on an essential governmental function of a sovereign State in the federal system.

The Court can and should entertain this motion to its original jurisdiction because a serious claim of grave constitutional magnitude can be shown as regards the rights of the State as State or as the State representing the rights of its political subdivisions. The original jurisdiction of the Supreme Court is the only forum which can adequately redress the injury of which South Carolina complains.

There is a complete lack of constitutional authority for the discriminatory classification of municipal obligations into a taxable form (bearer paper) and a nontaxable form (registered paper), as Congress was not granted power to tax the incidences of state sovereignty by either an original Constitutional grant or by the Sixteenth Amendment. As the express authority to tax the sovereign functions of a State is not granted in the Constitution, Congress is constitutionally precluded from the exercise of such power by the Tenth Amendment.

The Court should therefore grant original jurisdiction in the cause and find Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act an unconstitutional exercise of the taxing power of Congress.

## ARGUMENT

### I. South Carolina has presented a substantial constitutional claim over which the court should exercise its original jurisdiction.

A. The State as State is the real party in interest.

South Carolina has ably set forth in its brief supporting its Motion for Leave to File a Complaint (Brief of South Carolina at 34, 36, 39, 40) the imminent financial damage that the state will suffer if forced to comply with the provisions of Section 310(b)(1) of the Tax Equity and Fiscal Responsibility Act ("Section 310(b)(1)" of "TEFRA") requiring municipal securities be issued in registered as opposed to bearer form to retain their tax-exempt status. (Pub. L. No. 97-248, Tax Equity and Fiscal Responsibility Act of 1982, Section 310(b)(1).). The damage is imminent to every state in the federal system. By way of example, the Municipal Advisory Council of Texas (MAC), based on the charges of registrar banks as opposed to paying agent banks, has projected that costs of bond issuance will rise, depending on the size of the issue, between 1435% and 156%. See MAC Affidavit, Appendix. Further, financial damage will also result to the States with enforcement of Section 310(b)(1) due to increased costs of issuance: for example, filings of IRS Form 1099, not previously required, added costs of including registrar agreements for disclosure purposes in Official Statements, and higher interest rates. See Affidavit of Indianapolis Controller, Appendix. As such, threatened implementation of the law and its effect on the States creates a controversy of sufficient merit and seriousness to invoke the Court's original jurisdiction. See *Massachusetts v. Mellon*, 262 U.S. 447 at 484 (1923). See also *Illinois v. City of Milwaukee*, 406 U.S. 91, 94 (1981).

In the opinion of the State of Texas, irreparable harm to sovereign state functions results from the Secretary of the Treasury's proposal to enforce a law passed with no constitutional authorization because such law affects the borrowing capacity of a State or its political subdivisions. It is undisputed that the Federal government has a co-equal power with the States which form the Federal

union to levy taxes, but there is nowhere granted the power to tax a fellow sovereign. *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429 at 584 (1895) states:

> "The federal government in its appropriate sphere is supreme: but the States within the limits of their powers not granted, or, in the language of the tenth amendment, 'reserved' are as independent of the general government as that government within its sphere is independent of the States."

While Section 310(b)(1) of TEFRA does not directly tax State and municipal borrowing, it does impose a tax on such obligations if issued in bearer form. This conflicts directly with the State performing its governmental objectives in the most economical fashion because a lower rate of interest is available if it issues its obligations in bearer form. Issuing debt is "an operation essential to the important objectives for which the government was created," for that debt is issued to enable the government to accomplish its governmental functions. In *Weston v. City Council of Charleston*, 27 U.S. (2 Pet.) 449, 467 (1829), the Court found to be an impermissible burden on the functions of a government, a tax on "an operation essential to the important objectives for which the government was created". With Section 310(b)(1) the Congress seeks to impose a tax on an aspect of such an operation—on municipalities' capital formation process. The power to tax those operations essential to the fundamental aspects of a state government, according to *Weston*, supra, does not lie in the original grant of taxing power to the United States government. See also *Memphis State Bank & Trust Company v. Riley C. Garner*, _____U.S._____, 51 U.S.L.W. 4104, 4105 (1983), finding unconstitutional a discriminatory state tax where the "economic but not the legal incidence of the tax falls on the Federal

Government" (Tennessee had levied a 3% tax on banks for income earned on Treasury obligations, but not on Tennessee obligations) and *Washington v. United States,* _____U.S._____, 51 U.S.L.W. 4305 (1983).

Just as clearly, no such power is granted by the Sixteenth Amendment to the United States Constitution. While that amendment provides that "Congress shall have the power to tax all income from whatever source derived", it was intended to enable the Federal government to levy income tax, not a tax on essential objectives of its fellow sovereigns. The States, in fact, were assured at the time of passage that the Sixteenth Amendment was not intended to convey power to tax the States. 45 Cong. Rec. 1696 (1910). See also Goldberg, Arthur Abba, *A Call to Action: State Sovereignty, Deregulation and the World of Municipal Bonds,* 13 Urban Lawyer 253, 258, 259 (1981). Congress has twice proposed an *additional* constitutional amendment to end the exemption of interest on state obligations from federal income taxation with no success. 65 Cong. Rec. 43, 347 (1924) and 76 Cong. Rec. 3588 (1933). Congress has similarly been unsuccessful in repealing the statutory exemption on interest earned on state and municipal securities granted in Act of October 3, 1913, ch. 166, 38 Stat 168. Attempts at repeal failed in 1922, 1923, 1924, 1938, 1942, 1949, 1951, 1954 and 1959. Goldberg, supra at 259.

By what authority then, does the Secretary of the Treasury enforce a law with no colorable claim to constitutional authorization? Congress, after all, has only those powers explicitly granted by the Constitution; all others are reserved to the States and the people by operation of the Tenth Amendment. As the Court stated in *National League of Cities v. Usery,* 426 U.S. 833 at 845 (1976):

> We have repeatedly recognized that there are attributes of sovereignty attaching to every

> state government which may not be impaired by Congress, not because Congress may lack an affirmative grant of legislative authority to reach the matter, but because the Constitution prohibits it from exercising the authority in that manner.

It is the responsibility and duty of the States as States to protect their interests in this regard. The situation at hand is a challenge to just such interests.

B. The State has a real interest in the profound damage being done to the financing capacity of its political subdivisions.

The State must act to protect its political subdivisions' interests in financing essential governmental functions:

> A municipal corporation is the representative of the state and one of the instrumentalities of the state government.
>
> *Pollock,* supra, at 584

Municipalities of the State with the capacity to issue tax-exempt debt will suffer the same increased costs and other onerous burdens as the State if Section 310(b)(1) of TEFRA is allowed to go into effect. For smaller issuers, those with the least capacity to protect their interests, the costs of complying with registration will be proportionately higher than those of larger issuers. See MAC Affidavit, supra.

*Pollock,* quoting from *United States v. Baltimore & O.R.Co.,* 84 U.S. (17 Wall) 322 (1873) states that a municipal corporation is a creature of the State created to exercise a limited portion of the State's powers. *Pollock,* supra at 584. As municipalities of a State are its creatures, exercising a portion of the *State's* powers,

the State must and should be permitted to represent those subdivisions unconstitutionally deprived of their ability to exercise those powers.

## II. The Court is the only forum available which can do full equity to the claim of South Carolina.

The sovereign State of South Carolina has briefed the substantial financial costs and complications to its financing arrangements which will result from enforcement of Section 310(b)(1) of TEFRA. Brief of South Carolina, supra. The Court in *National League of Cities*, supra, at 254-256, dwelt at length on the constitutional infirmity of such financial burden on an essential state function. While standing may be available in other forums, incalculable financial damage will be done to an essential sovereign function if the matter is not expeditiously resolved. The Court is the only forum in which such treatment is possible.

Further, there is no other forum which can fulfill the test outlined by the Court for the exercise of its original jurisdiction. *Massachusetts v. Missouri*, 308 U.S. 1, 18 (1939). The test examines (1) "... the essential quality of the right asserted ..." and (2) "... whether recourse to that jurisdiction ... is necessary for the state's protection." See also *Illinois v. City of Milwaukee*, supra, *Washington v. General Motors Corp.*, 406 U.S. 109, 113 (1972) and *Maryland v. Louisiana*, _____U.S._____, 101 S.Ct. 2114, 2138 (1981) (dissent). In the situation at bar, the right of the first part of the test is the sovereign ability of a State to finance its integral governmental activities without unauthorized interference of its fellow sovereign. The second part is satisfied by the tremendous financial damage which will be done to the State before the issue can be resolved in another forum. If the Court refuses to entertain South Carolina's Motion, the damage done will be beyond any court's capacity to remedy it.

In refusing to entertain a motion to its original jurisdiction on the grounds of being an unsuitable forum in *Ohio v. Wyandotte Chemicals Corp.*, 401 U.S. 493, 499 (1971), the Court stated:

> ...we may decline to entertain a complaint brought by a State against the citizens of another State or country only where we can say with assurance that (1) declination of jurisdiction would not disserve any of the principal policies underlying the Article III jurisdictional grant and (2) the reasons of practical wisdom that persuade us that this Court is an inappropriate forum are consistent with the proposition that our discretion is legitimated by its use to keep this aspect of the Court's functions attuned to its other responsibilities.

The Court admitted that it had original jurisdiction, but, in this case, refused to exercise it on the basis that the principal purposes of the Article III jurisdictional grant could be served by a state court with concurrent jurisdiction. See 401 U.S. at 500. The *Ohio* case dealt with state law questions and common law nuisance doctrine, not with important problems of federal law as to which the Court stated "... we are the primary overseers." See 401 U.S. at 497, 498.

The Court in *Ohio* further found that as a primarily appellate tribunal it was ill-equipped to deal with a dispute which was "not so much the law as the facts." See 401 U.S at 503, 504. The issue at question in South Carolina's motion is not a factual question; it is a question of law, which would in any event be determined by the judge in a trial court: Is there, as a matter of law, constitutional authority for the implementation of Section 310(b)(1) of TEFRA?

As delineated above and in South Carolina's brief, there is no other court in this instance which can properly fulfill the purpose of the Article III jurisdictional grant. It is respectfully submitted that if the Court follows its own tests outlining appropriate cases in which to exercise its original jurisdiction, it will reach the conclusion that, as the only available forum with the power to do full equity to the claim, it must accept jurisdiction of South Carolina's action.

**III. Implementation of Section 310(b)(1) of TEFRA is an unconstitutional exercise of the otherwise legitimate federal power to tax.**

This Court's latest analysis of the limits placed on exercise of an otherwise legitimate use of Congressional authority by the Tenth Amendment reiterates the test laid down in *Hodel v. Virginia Surface Mining & Reclamation Association, Inc.*, 452 U.S. 264, 286-288 (1981). Such authority will be limited with showings:

> (1) ...that the challenged statute regulates the States as States.
> (2) that the regulation addressed matters that are indisputable attributes of state sovereignty.
> (3) that compliance with the statute would directly impair the ability of the State to structure integral operations in areas of traditional governmental functions.
> (4) that, assuming the challenged statute meets all the above requirements, the importance of the federal interests outweighs the impairment of state sovereignty.
>
> Equal Employment Opportunity Commission v. Wyoming, _____ U.S._____, 51 U.S.L.W. 4219, 4220, (1983)

As to the first prong of the test, there is clear regulation of the State as State in the present situation. While the incidence of the tax falls on the holder of the bond issued in bearer form, the injury done to the State by virtue of increased borrowing costs can "fairly be traced to the challenged action of the defendant." *Maryland v. Louisiana*, supra, quoting *Simon v. Eastern Kentucky Welfare Rights Organization*, 426 U.S. 26, 41-42 (1976). See also *Memphis State Bank*, supra. If the State issues obligations in registered form, it will be burdened with increased costs of issuance including higher rates of interest. Brief, supra, at I(A). See also Affidavit of Indianapolis, supra. If the State issues obligations in bearer form, they will be taxable, and, as such, will have to bear a higher rate of interest to be marketable.[1] Thus, the effect of the proposed regulation will, in either situation, increase the costs of the State's borrowing. The classification established by Section 310(b)(1) will impermissibly affect the States and their political subdivisions whether they choose to issue registered or bearer paper.

For example, the City of Indianapolis, faced with the prospect of having to issue all its obligations in registered form, decided to issue a series of fully registered park bonds. The syndicate manager eventually sold all the bonds, but Indianapolis ended up with interest costs about forty basis points higher than it would have had with bearer bonds—in absolute terms, increased interest costs of about $301,000 over the life of the bonds. Affidavit of Indianapolis, supra.

One need only multiply this figure by the number of municipal issuers of bearer bonds and the number of times they go to market annually to arrive at some no-

1. Because no tax has been imposed by the federal government on interest earned on state and local government obligations, these instruments have traditionally been marketed at interest rates below conventional interest rates.

tion of the increased expense in interest costs alone. It is no answer to say that the problem will correct itself when no issuer can issue bearer paper, for, as South Carolina's brief points out, there will be bearer bonds which already have been issued in the marketplace for decades to come. Texas argues further that even if bearer paper is eventually replaced by registered paper, it will be more costly than the continued use of *tax-exempt* bearer paper. Supra at 9. See Affidavit of Indianapolis, supra and Affidavit of MAC, supra.

That the second prong of the test is met is indisputable. How is a State to exercise any attribute of state sovereignty without the power to finance that attribute? If a State extends the right to an education, it must have money to build schools. If a State would enforce its penal laws, it must have money to build jails.[2] In upholding a tax on capital gains from trading in municipal bonds as not impairing state sovereignty, this court nevertheless affirmed that a tax on state obligations *per se* was constitutionally prohibited as a tax upon a State's borrowing power, a tax forbidden by the very concept of a federal system of government. See *Wilcutts v. Bunn*, 282 U.S. 216, 224-225 (1931).

In addition to the effects outlined in addressing prongs one and two of the Court's test for those regulations which must fall under the Tenth Amendment (most of those effects also going to prong three), Texas submits for the Court's consideration that increased costs of borrowing will "impair the ability of the State to 'structure integral operations in areas of traditional governmental functions'", *Hodel*, supra, at 287-288,

2. In Texas, the financial aspects of these attributes of state sovereignty are delegated to political subdivisions, but those subdivisions, too, suffer the same disability as the State: they must have money to perform the attributes of state sovereignty they are commanded by state law to implement.

*EEOC*, supra, at 4222. When the State and its subdivisions must pay more to meet their borrowing needs, there will be less available money to finance their operating costs. What is the profit to a town of building a new fire station, if, due to increased costs of borrowing, it can neither afford to purchase a fire truck nor pay the salaries of personnel to man the station? There is no use in a school without teachers. A prison without guards would hardly serve the purpose of incarcerating wrongdoers.[3] The greater the amount of money which must be raised to meet increased borrowing costs, the less money will be available for other governmental functions. See *National League of Cities*, supra, at 254-256.

Finally, the fourth part of the test which the Court reaffirmed in *EEOC*, supra—that the extent of the Federal interest advanced justifies the impairment to state sovereignty—is failed by the threatened implementation of Section 310(b)(1) of TEFRA. There is a question as to Federal interest at all. The position of the State of Texas is that the tax-exempt instances of State and local borrowing is a constitutional right. See, Brief, supra, Section I(A). Because the tax-exemption on the interest of State and local obligations is a matter of constitutional right, there can be no Federal interest at all in revenues lost to the Treasury by reason of the tax-exemption. If there is no Federal interest at all, there can be no constitutional impairment of state sovereignty given that the first three prongs of the test are met.

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3. It should be noted that virtually every prison facility in the State of Texas is under federal mandate to improve its conditions. See *Ruiz v. Estelle*, 503 F.Supp. 1265 (S.D. Tex. 1980), affirmed 650 F.2d 555 (5th Cir. 1981). This must include expansion of the facilities themselves. Once the money is borrowed to expand those facilities, there must yet be money left to improve the facilities, to provide more humane conditions of incarceration.

Assuming, *arguendo*, that there is a Federal interest, the State of Texas asserts that it is not of sufficient magnitude to impair such a fundamental aspect of state sovereignty. On November 20, 1982, the Joint Economic Committee of Congress released a Treasury Department study stating that the tax exemption on municipal bond interest "costs" Treasury $4.6 billion a year in "lost" individual income tax. However, the purported loss in tax revenue was only ranked tenth in total cost to the Treasury with the deduction for state and local taxes costing $26.5 billion, property tax deductions for owner-occupied homes costing $8.6 billion and other state and local tax write-offs costing $17.8 billion. *The Weekly Bond Buyer,* November 29, 1982, at 1 and 95. When Treasury itself ranks this "loss" of revenue tenth in importance, there is difficulty in ascertaining how the Federal interest can outweigh such an integral aspect of state sovereignty as the power to finance a State's governmental functions. There are at least three other sources of income noted above upon which Treasury could act first and "recover" more revenue, three deductions more clearly within the federal purview to disallow, at least within the constraints of the Tenth Amendment.

In *E.E.O.C.*, supra, the Court stressed that, in line with the holding in *National League of Cties,* supra, and *F.E.R.C. v. Mississippi,* 456 U.S. 742, 769-770 (1982), the degree of Federal interference with state sovereignty was the standard for determining an impermissible Tenth Amendment violation even when the Federal law 'directly impairs the States' ability to structure their integral operations' 51 U.S.L.W. at 4222. Even in striking down Wyoming's mandatory retirement age for game wardens and concluding that the Federal intrusion was not such an intrusion as to offend the Tenth Amendment, the Court stated that in some situations

> A State's employment relationship with its workers can...be one vehicle for the exercise of its core sovereign functions.
>
> 51 U.S.L.W. at 4222, n.11

The degree of interference was found permissible, not interference in all cases.

The implementation of Section 310 (b)(1), on the other hand, operates directly on a "core sovereign function" by regulating the essential sovereign power of the States to finance their governmental functions. There is no question that a State's financing is "one vehicle for the exercise of its core sovereign functions". Without financing a State would not be able to perform any "core sovereign function". There is a major difference between a State making an arbitrary decision that a game warden is unfit to fulfill the responsibilities assigned him after age fifty-five or sixty-five and a State making decisions in an attempt to finance its governmental functions at the lowest cost and with the least burden on its resources.

In addition to the "lost revenue" it associates with the tax exemption of interest on municipal bonds, the Treasury Department seems to have articulated a concern about the use of municipal bonds for the laundering of money from illegal transactions and to pass, untaxed, funds otherwise subject to taxation (notably, the passing of bearer bonds on death of the holder to an intended heir without passing the bonds through the decedent's taxable estate). *The Weekly Bond Buyer*, December 27, 1982, at 3. Texas submits that the Federal government has not demonstrated a sufficient Federal interest to punish States, in the face of the increased burden on the finances of every issuer of bearer bonds, for a use of their paper which is no fault of their own.

There can be no serious question that the Federal government has a substantial interest in preventing the avoidance of lawfully levied taxes. A solution should be found, however, that does not cause virtually as much financial damage to its innocent fellow sovereigns as it corrects for the Federal government. Through the vehicle of the Fifth Amendment, this Court has found the Federal government subject to similar constraints of equal protection and due process applicable to the States through the Fourteenth Amendment. See *Bolling v. Sharpe*, 347 U.S. 497 (1954). In the balancing of interests herein shown, Texas submits that the interests of the Federal government are out-weighed by the profound damage which will be inflicted on the system of federalism.

The Court recently held that a state tax on banks for interest earned on Treasury obligations was an impermissible burden on Federal borrowing costs, where banks were not taxed on interest earned on State obligations. *Memphis Bank & Trust*, supra. While the Court noted that such a tax was permissible if non-discriminatory, because the tax was not levied directly on the Federal government, the Court found that Tennessee here had enacted a law which discriminated against Federal obligations in favor of those of the State of Tennessee. Section 310(b)(1) of TEFRA similarly discriminations in favor of registered as opposed to bearer obligations. Treasury is placing an impermissible burden on State borrowing costs. Brief, supra, at I(A) and III. Affidavit of Indianapolis, supra. Affidavit of MAC, supra. Brief of South Carolina, supra, at 41, n.11. The Court expressed concern that if all fifty states were to enact such a law, the additional borrowing costs of the United States would be as much as $280 million. *Memphis Bank*, supra, at 4105, n. 8.

Section 310(b)(1) is a law which does affect fifty States and their countless political subdivisions. Texas sub-

mits that based on the experience of Indianapolis, the cost of this discriminatory law is likely to exceed the $280 million considered important in *Memphis Bank*. Affidavit of Indianapolis, supra. See also Affidavit of MAC. If there is any meaning left in the concept of federalism, Congress should not in this case be allowed to enact a law having the same effect as one which this Court found constitutionally prohibited to a State.

## CONCLUSION

For the reasons above outlined the sovereign State of Texas urges that the Court grant South Carolina's Motion to the Court's original jurisdiction. As the Court stated in *Georgia v. Pennsylvania R. Co.*, 324 U.S. 439, at 466 (1971):

> Once a state makes out a case which comes within our original jurisdiction, its right to come here is established. There is no requirement in the Constitution that it go further and show that no other forum is available to it."

While practical considerations have narrowed the scope of that statement, it is demonstrated in South Carolina's brief and in the argument of the State of Texas that such considerations are not here applicable and the gravity of the imminent harm to the financing needs of all fifty States (and their political subdivisions and citizens) require that the Court accept original jurisdiction as the only acceptable forum.

The State of Texas has also demonstrated that the tremendous adverse financial impact of Section 310 (b)(1) on essential governmental functions of a sovereign State and its political subdivisions is without constitutional authorization. The proposed implementation of Section 310(b)(1) fails under every constitutional test:

the original grant of taxing power in the Constitution, the Sixteenth Amendment and the Tenth Amendment. A law with no constitutional authority is a law which cannot stand. "The question in this case is purely one of constitutional power", *E.E.O.C.*, supra, (Steven's concurrence) at 4226. That constitutional power simply does not exist.

The State of Texas would direct the Court's attention to the Defendant's own words on the subject of Federal taxation of municipal bonds as reported in The Weekly Bond Buyer, April 25, 1983 at 5:

> Mr. Regan said after giving testimony in Congress that "you would have to change the constitution" to impose a tax on municipal issues.

Respectfully submitted,

JIM MATTOX
Attorney General of Texas

DAVID R. RICHARDS
Executive Assistant

ROBERT T. LEWIS
Assistant Attorney General

MICHAEL CAFISO
Assistant Attorney General

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**SUSAN LEE VOSS**
**Assistant Attorney General**

**Attorney General of Texas**
**P.O. Box 12548**
**Austin, Texas 78711**
**(512) 475-4651**

**May _____, 1983**

## CERTIFICATE OF SERVICE

I, SUSAN LEE VOSS, an Assistant Attorney General for the State of Texas and a member of the Bar of the Court, do hereby certify that, in accordance with Rule 28.4(a), three (3) copies of the Amicus Curiae Brief in the matter of *South Carolina v. Regan* were served on all parties required to be served on this date by depositing same in the United States mail, first-class postage prepaid, and addressed as follows: The Honorable William French Smith, Attorney General of the United States, Department of Justice, 10th and Constitution Avenue N.W., Washington, D.C. 20530, The Honorable Rex E. Lee, The Solicitor General of the United States, Department of Justice, Washington, D.C. 20530; The Honorable Donald T. Regan, Secretary of the United States Treasury, Department of the Treasury, 1500 Pennsylvania Avenue, N.W., Washington, D.C. 20220; The Honorable T. Travis Medlock, Attorney General of the State of South Carolina, P.O. Box 11549, Columbia, South Carolina 29211; and The Honorable Richard W. Riley, Governor of the State of South Carolina, P.O. Box 11450, Columbia, South Carolina 29211.

This _____ day of May, 1983.

SUSAN LEE VOSS
Assistant Attorney General

P.O. Box 12548
Austin, Texas 78711

# APPENDIX

No. 94, Original

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

State of South Carolina,

*Plaintiff,*

VS.

Donald T. Regan, Secretary of
the Treasury of the United States
of America,

*Defendant.*

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## AFFIDAVIT OF DANNY BURGER

State of Texas §
§
County of Travis §

Before me, the undersigned Notary Public, on this day personally appeared Danny Burger, known to me, and after being by me duly sworn on his oath deposed and said:

1. I am Executive Director of the Municipal Advisory Council of Texas, Inc. (hereinafter referred to as "Municipal Advisory Council"). The Municipal Advisory Council is a non-profit association made up of persons and entities involved in the business of underwriting, buying, and selling bonds and securities.

2. I have worked and been actively involved in the Texas bond business for over twenty-five years. From 1957 to 1963, I was a senior bond analyst with the

Municipal Advisory Council. From 1963 to 1968, I was the Municipal Bond Portfolio Manager for the American National Insurance Company, located in Galveston. From 1968 to 1976, I was the Development Fund Manager for the Texas Water Development Board, where I supervised the State bond program for water and sewer services. From 1976 through the present, I have been the Executive Director for the Municipal Advisory Council.

3. The Municipal Advisory Council, in the regular course of its business, maintains records of the number, kind, and size of all tax-exempt bond issues made in the State of Texas by State agencies and political subdivisions of the State. Attached to the Affidavit as Exhibit 1 is a summary of the tax-exempt bond issues made in the State of Texas during the period from January 1, 1982, through November 26, 1982. As this Exhibit reflects, fifty-seven percent of all issues were of sizes less than $2.5 million. Based on my knowledge and experience in the Texas bond business, I believe that the overwhelming majority of these tax-exempt issues were made by small political subdivision-issuers, including municipalities, school districts, hospital authorities, river authorities, and so forth.

4. Through both my position as Executive Director of the Municipal Advisory Council and my general knowledge of the Texas bond industry, I am aware of fees typically charged to issuers by paying agents. A "paying agent" is that entity, almost always a bank or other financial institution, designated by the issuer as its agent for the payment of principal and interest on the bonds to the bondholders. Attached to this Affidavit as Exhibit 2, in the third column from the left, are the average fees charged to issuers by Texas paying agents at the present time.

5. In my capacity as Executive Director of the Municipal Advisory Council, I am also involved with

representatives from all areas of the bond industry, including political subdivisions (in their capacity as issuers) and financial institutions (in their capacity as paying agents), in helping to gather information and develop guidelines for use in the implementation of the TEFRA bond registration requirement. Through such work as well as through my own experience in the industry, I believe that the projected fees set forth in the fourth column on Exhibit 2 are typical of the fees projected by Texas financial institutions that will serve as both the paying agent and the registrar for registered bonds. The reason that such large cost increases are projected is because of the enormous increases in computer equipment, paperwork and personnel necessary to handle fully registered bonds.

6. Because the bond registration requirement will most adversely affect small bond issues and because the majority of tax-exempt bond issues in Texas are small in size, the bond registration requirement will have a significant economic impact on political subdivisions in Texas issuing tax-exempt bonds.

7. Based on my experience in the bond business, I believe that issuers will pay increased interest rates in order to issue fully registered bonds. An increase in interest rates means that the issuers must make higher annual interest payments over the life of the bonds, resulting, for example, in higher taxes and service rates. An increase in interest rates also means difficulties for issuers ever issuing such bonds at all depending on bond market conditions at the time, for example, during a period of high interest rates.

8. Increased costs incurred by issuers that are associated with higher interest rates will be significantly higher that the increased costs resulting from the projected fees set forth in Exhibit 2. In 1982, by assuming only a slight one-half of one percent (½ of 1%) increase in interest rates per issue, the total increased interest costs to the issuers would exceed $20,000,000.

This figure is determined by multiplying the January-November 1982 volume, $4,369,565,000 (see Exhibit 1), times the one-half of one percent increase in interest rates.

I have personal knowledge of the facts alleged herein. I declare under penalty of perjury that the foregoing is true and correct.

Danny Burger

Subscribed and sworn to before me this the 30th day of March, 1983.

/s/ Gloria P. Carter

Notary Public in and for the State of Texas

My Commission Expires: Jan. 25, 1984

# EXHIBIT 1
## SUMMARY OF TAX-EXEMPT BOND ISSUES IN TEXAS
(January 1, 1982 - November 26, 1982)

| Issue Size | Texas Issues | Volume of Bonds | Cumulative Percent of Issues |
|---|---|---|---|
| $ 1,000,000 | 196 | $ 88,213,000 | 36.0% |
| 2,500,000 | 127 | 215,730,000 | 57.0% |
| 5,000,000 | 98 | 362,978,000 | 75.0% |
| 7,500,000 | 42 | 266,443,000 | 82.0% |
| 10,000,000 | 26 | 235,341,000 | 87.0% |
| 25,000,000 | 46 | 740,860,000 | 95.0% |
| 87,857,000* | 28 | 2,460,000,000 | 100.0% |
| | 563 | $4,369,565,000 | |

*Average size based on volume divided by issues.

# EXHIBIT 2

## COMPARISON OF CURRENT PAYING AGENT FEES WITH PROJECTED PAYING AGENT/REGISTRAR FEES

| Issue Size | Cumulative Percent of Issues (See Exhibit 1) | Current Annual Paying Agent Fees (Average) | Projected Annual Paying Agent/Registrar (Average) | Projected Annual Percent Increase in Fees |
|---|---|---|---|---|
| $1,000,000 | 36.0% | 100 | $2535.00 | 1435% |
| 2,500,000 | 57.0% | 200 | 2570.00 | 1185% |
| 5,000,000 | 75.0% | 400 | 2640.00 | 560% |
| 7,500,000 | 82.0% | 600 | 2780.00 | 363% |
| 10,000,000 | 87.0% | 800 | 3060.00 | 282% |
| 25,000,000 | 95.0% | 2000 | 5000.00 | 156% |

STATE OF INDIANA )
)SS:
COUNTY OF MARION)

AFFIDAVIT

Fred L. Armstrong, being first duly sworn upon his oath, deposes and says:

1. That he is the duly appointed, qualified and acting Controller, the City of Indianapolis, Indiana, and as such is responsible for and oversees the issuance and sale of general obligation bonds of the City of Indianapolis and of the special taxing districts of the City.

2. That the payments of the principal of and the interest on general obligation bonds of the City and of its special taxing districts are secured by a pledge of ad valorem property taxes levied on property located within the City or within the special taxing districts as the case may be.

3. That in 1982 the Park District of the City of Indianapolis ("Park District"), a special taxing district comprising all of Marion County, Indiana, and empowered by state law to issue and sell general obligation bonds of the district for the purpose of financing park improvements, initiated proceedings for the issuance of Park District Bonds in the aggregate principal amount of $7,500,000 (the "Bonds").

4. That the Bonds were originally intended to be isssued in bearer form (as had all previous general obligation bonds of the City and its special taxing districts) until the passage by Congress of the Tax Equity and Fiscal Responsibility Act of 1982 (the "Act"), which Act, inter alia, requires such bonds to be issued in registered form in order for the interest on such bonds to be exempt from the federal income tax, whereupon the

Park District undertook such proceedings as would enable the Bonds to be sold as registered bonds.

5. That prior to the sale of the Bonds, Congress postponed the effective date of the mandatory registration provisions of the Act to July 1, 1983.

6. That the Park District chose to proceed to sell the Bonds in fully registered form rather than to incur additional costs and delays which would have been occasioned had the Park District decided to take further legal proceedings required to sell the bonds in bearer form.

7. That the Bonds were sold at public sale to the highest qualified bidder on January 26, 1983 at a price of par and bearing interest at a net effective average annual interest rate of 8.624754%.

8. That subsequent to the sale of the Bonds he learned that the fact that the Bonds were issued in fully registered form caused bidders for the Bonds to quote higher interest rates for the bonds than they would have quoted had the Bonds been issued in bearer form.

9. That he contacted City Securities Corporation through its Executive Vice-President, Mr. Richard DeBolt, and asked him to investigate and determine from the managers of the successful bidding account the amount of the increase in the interest cost to the City which was attributable to the fact that the Bonds had been issued in fully registered form.

10. That Mr. DeBolt reported his findings in a letter dated March 8, 1983, a true and accurate copy of which is attached hereto and incorporated herein by reference as Exhibit "A", and said letter demonstrates that the fact that the Bonds were issued in fully registered form rather than in bearer form resulted in an increased interest cost to the City of between 25 basis points (0.25%) and 50 basis points (0.50%).

11. That based upon the statements set forth in Exhibit "A" he has computed the dollar interest cost attributable to the fact that the Bonds were issued in fully registered form and he estimates that the taxpayers of the Park District will be forced to pay an additional $301,000 in interest costs over the 15 year life of the bond issue that they would not have had to pay if the Bonds had been issued in bearer form.

12. In addition to the increased interest costs associated with the registered Bonds, he has had to contract with a local bank to serve as registrar and paying agent on the Bonds, and he estimates that the average annual expense to the taxpayers for these services during the life of the bond issue will be $5,000 for a total of $75,000 for the fifteen year life of the Bonds.

Further affiant saith not.

/s/

Fred L. Armstrong
Controller, City of Indianapolis, Indiana

Subscribed and sworn to before me, a Notary Public, in and for said County and State this 30th day of March, 1983.

Signed /s/

Printed Shannon Thompson

NOTARY PUBLIC

County of Residence: Marion

My Commission Expires: October 14, 1984

EXHIBIT "A"

March 8, 1983

Mr. Fred Armstrong
City Controller
City-County Building
Indianapolis, IN. 46204

RE: $7,500,000 Indianapolis Park District
Fully Registered Bond Issue

Dear Fred:

I called the managers of the successful bidding account on this issue and asked them to comment on the difference in interest cost they believed existed between this registered issue and the cost if it had been issued in coupon form. The following comments were made:

> Randall Coleman, Vice President in charge of Underwriting, Smith Barney - Chicago (Lead Manager). Thought you were penalized 25 to 40 basis points. Probably closer to 40. A letter to this effect was written to you. He can be quoted.
>
> William Wingader, Vice President, Manager, Underwriting Dept., John Nuveeen & Company

(Co-manager). Cost to issuer a minimum of 25 but probably 40 basis points on original issue. The account sold the last 200,000 to 300,000 of the issue at a loss of 75 basis points which relates to a loss of about $60.00 per 1,000. He believes the registration was the reason the bonds had to be sold at a loss. He also stated that between the time the issue was purchased by the Smith Barney group and the sale of the remaining bonds, the market had improved by about 50 basis points which adds further to the adverse effect of the registrations. He can be quoted.

James Arkebauer, Vice President, Manager Underwriting Dept., First Wisconsin National Bank of Milwaukee (Co-Manager). They dropped from the account and did not bid on the issue because of the difficulty they have found in selling registered bonds. He stated he thought the registration cost the District at least 50 basis points. He also stated a State of Wisconsin registered issue trades in the secondary market at a 75 bais points penalty to the State's coupon issues. Also two City of Milwaukee General Obligation issues sold at the same time. One because the funds were to be used for housing, was required to be registered. The other sold in coupon form. The registered issue received a bid with a 25 basis point increase in cost to the City. Now in secondary market trading, the coupon issue sells at a 75 basis points premium above the registered issue. He can be quoted.

Edward Swanton, Vice President, National Underwriting Manager, Merrill Lynch White Weld Capital Markets Group, New York (Co-Manager). He did not want to be quoted but

finally admitted that he thought the registration cost the Park District about 25 basis points.

All these comments show that the Park District interest cost was substantially higher because the bonds were sold in fully registered form.

I hope this will be of some help to you. If I can be of further service, please call.

Sincerely,

Richard H. DeBolt
Executive Vice President

RHD/rsl